

**Montabella Community Schools
Edmore, Michigan**

FINANCIAL STATEMENTS

June 30, 2006

Montabella Community Schools

Edmore, Michigan

BOARD OF EDUCATION

June 30, 2006

Linda Binkley	President
Chris Rasmussen	Vice-President
Emily Longnecker	Secretary
Gregory Perkins	Treasurer
Dennis Stratton	Trustee
Jann LaPointe	Trustee
Bryan Smith	Trustee

Ronald L. Farrell	Superintendent
-------------------	----------------

Montabella Community Schools

TABLE OF CONTENTS

June 30, 2006

	<u>PAGE</u>
INDEPENDENT AUDITOR'S REPORT	i-ii
MANAGEMENT'S DISCUSSION AND ANALYSIS	iii-viii
FINANCIAL STATEMENTS	
District-wide Financial Statements:	
Statement of Net Assets	1
Statement of Activities	2
Fund Financial Statements:	
Governmental Funds Balance Sheet	3
Reconciliation of the Governmental Funds Balance Sheet to the Statement of Net Assets	4
Statement of Revenues, Expenditures, and Changes in Fund Balances - Governmental Funds	5
Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances of Governmental Funds to the Statement of Activities	6
Fiduciary Funds:	
Statement of Fiduciary Net Assets	7
Statement of Changes in Fiduciary Net Assets	8
Notes to Financial Statements	9-23
REQUIRED SUPPLEMENTARY INFORMATION	
Budgetary Comparison Schedule - General Fund	24-25
OTHER SUPPLEMENTARY INFORMATION	
Combining Balance Sheet - Nonmajor Governmental Funds	26-27
Combining Statement of Revenues, Expenditures, and Changes in Fund Balances - Nonmajor Governmental Funds	28-29
REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS	30

Principals

Dale J. Abraham, CPA
Michael T. Gaffney, CPA
Steven R. Kirinovic, CPA
Aaron M. Stevens, CPA
Eric J. Glashouwer, CPA



3511 Coolidge Road
Suite 100
East Lansing, MI 48823
(517) 351-6836
FAX: (517) 351-6837

INDEPENDENT AUDITOR'S REPORT

To the Board of Education
Montabella Community Schools
Edmore, Michigan

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Montabella Community Schools as of and for the year ended June 30, 2006, which collectively comprise the District's financial statements as listed in the table of contents. These financial statements are the responsibility of Montabella Community Schools' management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of Montabella Community Schools as of June 30, 2006, and the respective changes in financial position, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated August 3, 2006 on our consideration of Montabella Community Schools' internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The management's discussion and analysis and budgetary comparison information, as identified in the table of contents, are not a required part of the financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise Montabella Community Schools' financial statements. The accompanying other supplementary information, as identified in the table of contents, is presented for the purpose of additional analysis and is not a required part of the financial statements. The other supplementary information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

Abraham & Gaffney, P.C.

ABRAHAM & GAFFNEY, P.C.
Certified Public Accountants

August 3, 2006

Montabella Community Schools

MANAGEMENT'S DISCUSSION AND ANALYSIS

June 30, 2006

This section of the Montabella Community School's annual financial report presents our discussion and analysis of the School District's financial performance during the year ended June 30, 2006. Please read it in conjunction with the School District's financial statements, which immediately follow this section.

Using this Annual Report

This annual report consists of a series of financial statements and notes to those statements. These statements are organized so the reader can understand Montabella Community Schools financially as a whole. The **district-wide** financial statements provide information about the activities of the whole School District, presenting both an aggregate view of the School District's finances and a longer-term view of those finances. The **fund** financial statements provide the next level of detail. For governmental activities, these statements tell how services were financed in the short-term as well as what remains for future spending. The fund financial statements look at the School District's operations in more detail than the district-wide financial statements by providing information about the School District's most significant funds, the General Fund and the Site and Facilities Sinking Fund, with all other funds presented in one column as nonmajor funds. The remaining statements (the Statement of Fiduciary Net Assets and the Statement of Changes in Fiduciary Net Assets) present financial information about activities for which the School District acts solely as an agent for the benefit of students and parents. The structure of the financial statements is as follows:

Management's Discussion and Analysis (MD&A)
(Required Supplementary Information)

Basic Financial Statements

District-wide Financial Statements Fund Financial Statements

Notes to the Financial Statements

(Required Supplementary Information)
Budgetary Information for Major Funds

Other Supplementary Information

Reporting the School District as a Whole - District-wide Financial Statements

One of the most important questions asked about the School District is, "As a whole, what is the School District's financial condition as a result of the year's activities?" The statement of net assets and the statement of activities, which appear first in the School District's financial statements, report information on the School District as a whole and its activities in a way that helps you answer this question. We prepare these statements to include all assets and liabilities, using the accrual basis of accounting, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the School District's net assets - the difference between assets and liabilities, as reported in the statement of net assets - as one way to measure the School District's financial health or financial position. Over time, increases or decreases in the School District's net assets - as reported in the statement of activities - are indicators of whether its financial health is improving or deteriorating. The relationship between revenues and expenses is the School District's operating results. However, the School District's goal is to provide services to our students, not to generate profits as commercial entities do. One must consider many other non-financial factors, such as the quality of the education provided, the condition of the district's assets and the safety of the schools, to assess the overall health of the School District.

The statement of net assets and the statement of activities report the governmental activities for the School District, which encompass all of the School District's services, including instruction, support services, community services, athletics and food services. Property taxes, unrestricted State aid (foundation allowance revenue), and State and federal grants finance most of these activities.

Montabella Community Schools

MANAGEMENT'S DISCUSSION AND ANALYSIS

June 30, 2006

Reporting the School District's Most Significant Funds - Fund Financial Statements

The School District's fund financial statements provide detailed information about the most significant funds - not the School District as a whole. Some funds are required to be established by State law and by bond covenants. However, the School District establishes many other funds to help it control and manage money for particular purposes (the Food Service and Athletics Funds are examples) or to show that it is meeting legal responsibilities for using certain taxes, grants, and other money (such as bond-funded construction funds used for voter-approved capital projects). The governmental funds of the School District use the following accounting approach:

Governmental funds - All of the School District's services are reported in governmental funds. Governmental fund reporting focuses on showing how money flows into and out of funds and the balances left at year-end that are available for spending. They are reported using an accounting method called modified accrual accounting, which measures cash and all other financial assets that can readily be converted to cash. The governmental fund statements provide a detailed short-term view of the operations of the School District and the services it provides. Governmental fund information helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the School District's programs. We describe the relationship (or differences) between governmental activities (reported in the statement of net assets and the statement of activities) and governmental funds in reconciliations.

The School District as Trustee - Reporting the School District's Fiduciary Responsibilities

The School District is the trustee, or fiduciary, for its student activity funds and private purpose trust funds. All of the School District's fiduciary activities are reported in separate statements of fiduciary net assets and changes in fiduciary net assets. We exclude these activities from the School District's other financial statements because the School District cannot use these assets to finance its operations. The School District is responsible for ensuring that the assets reported in these funds are used for their intended purposes.

The School District as a Whole

Recall that the statement of net assets provides the perspective of the School District as a whole. Table 1 provides a summary of the School District's net assets as of June 30, 2006 with comparative information as of June 30, 2005:

Table 1

	Statement of Net Assets <u>June 30, 2006</u>	Statement of Net Assets <u>June 30, 2005</u>
Assets		
Current and other assets	\$ 3,794,307	\$ 4,008,394
Capital assets, net of accumulated depreciation	<u>12,717,605</u>	<u>13,082,294</u>
Total Assets	16,511,912	17,090,688
Liabilities		
Current Liabilities	2,872,934	3,188,344
Noncurrent Liabilities	<u>9,501,260</u>	<u>10,284,705</u>
Total Liabilities	12,374,194	13,473,049
Net Assets		
Invested in capital assets, net of related debt	2,703,024	2,310,562
Restricted	689,054	688,561
Unrestricted	<u>745,640</u>	<u>618,516</u>
	<u>\$ 4,137,718</u>	<u>\$ 3,617,639</u>

Montabella Community Schools

MANAGEMENT'S DISCUSSION AND ANALYSIS

June 30, 2006

The analysis in Table 1 focuses on the net assets of the district. The affect on net assets as a result of the fiscal year activities is reflected in Table 2.

The School District's net assets were \$3,617,639 at June 30, 2005 and \$4,137,718 at June 30, 2006 (Table 1). Net assets have increased by \$520,079.

Capital assets, net of related debt totaling \$2,703,024 compares the original cost, less depreciation of the School District's capital assets, to long-term debt used to finance the acquisition of those assets. Capital assets also reflect investments in capital assets from operating funds. Most of the debt will be repaid from voter-approved property taxes collected as the debt service comes due. Durant loan obligations of the State are included in Long-Term obligations of the School District. Restricted net assets are reported separately to show legal constraints from debt covenants and enabling legislation that limit the School District's ability to use those net assets for day-to-day operations. Restricted Net Assets reflect the Debt Service fund balances less accrued interest on long-term debt as of June 30, 2006 in the amount of \$232,465 and the fund balance of the Site and Facilities Sinking Fund in the amount of \$456,589. Unrestricted Net Assets reflect those assets available to the school district for use in its operation.

The \$745,640 in unrestricted net assets of governmental activities represents the *accumulated* results of all past years' operations. The unrestricted net assets balance enables the School District to meet working capital and cash flow requirements as well as to provide for future uncertainties. The operating results of the General Fund will have a significant impact on the change in unrestricted net assets from year to year.

The results of this year's operations for the School District as a whole are reported in the condensed statement of activities (Table 2), which shows the changes in net assets for fiscal year 2005/06.

Table 2

	Fiscal Year Ended June 30, 2006	Fiscal Year Ended June 30, 2005
Revenue		
Program Revenue:		
Charges for services	\$ 230,616	\$ 253,520
Operating Grants	1,668,848	1,630,936
Capital Grants	47,207	11,760
General Revenue:		
Property Taxes	2,425,311	2,136,296
School state aid - unrestricted	5,727,559	5,740,999
Other	<u>211,523</u>	<u>187,085</u>
Total Revenue	10,311,064	9,960,596
Functions/Program Expenses		
Instruction	4,948,611	4,834,521
Support Services	3,271,599	3,109,873
Food Service	445,582	475,321
Athletics	208,661	169,452
Transfers to other districts	131,416	148,624
Interest and costs on long-term debt	212,455	562,601
Unallocated depreciation	<u>572,661</u>	<u>566,311</u>
Total Expenses	<u>9,790,985</u>	<u>9,866,703</u>
Increase in Net Assets	<u>\$ 520,079</u>	<u>\$ 93,893</u>

Montabella Community Schools

MANAGEMENT'S DISCUSSION AND ANALYSIS

June 30, 2006

As reported in the Statement of Activities, the cost of all of our *governmental* activities this year was \$9,790,985. Certain activities were partially funded from those who benefited from the programs (\$230,616 charges for services) or by other governments and organizations that subsidized certain programs with operating and capital grants and contributions (\$1,716,055). We paid for the remaining "public benefit" portion of our governmental activities with \$2,425,311 in taxes (for General & Debt Service funds) and \$5,939,082 in State foundation allowance and other revenues, i.e., interest and general entitlements.

As discussed above, the net cost shows the financial burden that was placed on the State and the School District's taxpayers by each of these functions. Since property taxes for operations and unrestricted State aid constitute the vast majority of district operating revenue sources, the Board of Education and administration must annually evaluate the needs of the School District and balance those needs with State-prescribed available unrestricted resources.

The School District's Funds

As we noted earlier, the School District uses funds to help it control and manage money for particular purposes. Looking at funds helps the reader consider whether the School District is being accountable for the resources taxpayers and others provide to it and may provide more insight into the School District's overall financial health.

As the School District completed this year, the governmental funds reported a combined fund balance of \$1,463,309, which is an increase of \$4,890 from last year.

In the General Fund, our principal operating fund, the fund balance increased \$2,908 to \$649,213. General Fund fund balance is available to fund costs related to allowable school operating purposes. Montabella Community Schools uses its Fund Balance to "smooth" unexpected changes in revenues and/or expenditures.

Our Special Revenue Funds fund balances increased \$16,740 to \$37,628. Special Revenue Funds include the Food Service and Athletics Funds.

The Debt Service Funds showed a fund balance decrease of approximately \$53,721, and the Capital Projects Funds fund balances increased by \$38,963.

General Fund Budgetary Highlights

Over the course of the year, the School District revises its budget as it attempts to deal with unexpected changes in revenues and expenditures. State law requires that the budget be amended to ensure that expenditures do not exceed appropriations. The final amendment to the budget was actually adopted just before year-end. A schedule showing the School District's original and final budget amounts compared with amounts actually paid and received is provided in required supplementary information of these financial statements.

General Fund Expenditures:

The District's budget for expenditures changed as follows during the year:

		<u>Percent</u>
Total Expenditures Original Budget	\$ 8,579,381	100.0
Total Expenditures Final Budget	<u>8,639,787</u>	<u>100.7</u>
Increase in Budget Expenditures	<u>\$ 60,406</u>	<u>0.7</u>

The District's actual expenditures were less than the final budget by \$102,420 or 1.2 percent.

Montabella Community Schools
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2006

Revenue Change from Original to Final Budget:

		<u>Percent</u>
Total Revenues Original Budget	\$ 8,526,063	100.0
Total Revenues Final Budget	<u>8,404,238</u>	<u>98.6</u>
Increase in Budget Revenues	<u>\$(121,825)</u>	<u>(1.4)</u>

The District's final actual general fund revenues differed from the final budget by \$72,455, a variance of (.8%) from the final budget.

Capital Assets and Debt Administration

Capital Assets

As of June 30, 2006, the School District had \$19,079,494 invested in a broad range of capital assets, including buildings and improvements, vehicles, and equipment. This amount represents a net increase (including additions and disposals) of \$207,671 from last year.

	<u>2006</u>	<u>2005</u>
Vehicles	67,788	68,089
Buildings and improvements	16,716,589	16,529,039
Equipment	<u>2,295,117</u>	<u>2,274,695</u>
Total historical cost	<u>\$ 19,079,494</u>	<u>\$ 18,871,823</u>

This year's additions of \$207,972 included office equipment and various building improvements. No new debt was issued for these additions.

Debt

At the end of this year, the School District had \$10,380,598 in bonds and other obligations outstanding versus \$10,823,987 in the previous year. Those obligations consisted of the following:

	<u>2006</u>	<u>2005</u>
General Obligation Bonds	\$ 10,260,000	\$ 10,690,000
Durant Resolution Bonds	69,435	75,127
Notes and Loans	1,605	6,605
Severance pay	<u>49,558</u>	<u>52,255</u>
Total	<u>\$ 10,380,598</u>	<u>\$ 10,823,987</u>

MANAGEMENT'S DISCUSSION AND ANALYSIS

June 30, 2006

Economic Factors and Next Year's Budgets and Rates

Our elected Board of Education and administration considered many factors when setting the school district's 2005/06 fiscal year budgets. The one most important and somewhat unpredictable factor is our student count. The State foundation revenue is determined by multiplying the blended count by the foundation allowance per pupil. The blended count for the 2006 year is established by a legislatively set percentage of the fall and winter counts. About 67% of the total general fund revenue is from the State foundation allowance. The school district can no longer access additional property tax revenue for general operations. This funding configuration makes the district funding heavily dependent on the State's ability to fund local school operations. Early enrollment projections at the beginning of the 2006/07 academic year indicate continuation of an ongoing decline in enrolment and likelihood of six to twelve fewer students than in the 2005/06 school year as well as twenty to twenty-five fewer students than were estimated in 2005/06 budgetary planning. Once the final count and related per pupil funding rate is established, State law requires the school district to amend the budget if actual district resources are not sufficient to fund original appropriations.

The school district's revenue is greatly dependent on State funding and the status of the State's School Aid Fund. The actual revenue received depends on the State's ability to collect revenues as projected to fund its appropriation to school districts. In fact, in two of the last four years and because of revenue shortfalls, the State was unable to fund schools in accordance with the School Aid Act and therefore necessarily discounted foundation allowance allocations. Other factors affecting the 2006/07 school year are increases in the health insurance and in the district contribution to the State retirement system. Changes in staffing, elevated costs to provide special education services, and increased costs for employee contracts likewise had impact on initial budget projections. Additional errors in reporting likewise caused previously unforeseen expenditures in the 2005/06 budget.

Contacting the District's Management

This financial report is intended to provide our taxpayers, parents, and investors with a general overview of the District's finances and to show the District's accountability for the money it receives. If you have any questions about this report or need additional information, we welcome you to contact the Montabella Community Schools central office which is located at 302 West Main Street, Edmore, Michigan.

BASIC FINANCIAL STATEMENTS

Montabella Community Schools

STATEMENT OF NET ASSETS

June 30, 2006

	Governmental Activities
ASSETS	
Current assets	
Cash and cash equivalents	\$ 2,405,776
Accounts receivable	2,332
Due from other governmental units	1,268,026
Inventories	9,751
Prepays	2,500
	<hr/>
Total current assets	3,688,385
Noncurrent assets	
Deferred charges, net of ammortization	105,922
Capital assets, net of accumulated depreciation	12,717,605
	<hr/>
Total noncurrent assets	12,823,527
	<hr/>
TOTAL ASSETS	16,511,912
LIABILITIES	
Current liabilities	
Accrued payroll	371,974
Other accrued liabilities	270,291
Due to other governmental units	327,811
Short-term note payable	1,255,000
Current portion of accrued interest	75,506
Current portion of accrued severance payable	12,389
Current portion of long-term debt	559,963
	<hr/>
Total current liabilities	2,872,934
Noncurrent liabilities	
Noncurrent portion of accrued interest	9,473
Noncurrent portion accrued severance payable	37,169
Noncurrent portion of long-term debt	9,454,618
	<hr/>
Total noncurrent liabilities	9,501,260
	<hr/>
TOTAL LIABILITIES	12,374,194
NET ASSETS	
Invested in capital assets, net of related debt	2,703,024
Restricted for debt service	232,465
Restricted for sinking fund activity	456,589
Unrestricted	745,640
	<hr/>
TOTAL NET ASSETS	\$ 4,137,718
	<hr/>

See accompanying notes to financial statements.

Montabella Community Schools

STATEMENT OF ACTIVITIES

Year Ended June 30, 2006

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenues and Changes in Net Assets
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	
Governmental activities					
Instruction	\$ 4,948,611	\$ 7,295	\$ 1,215,096	\$ 20,018	\$ (3,706,202)
Supporting services	3,271,599	35,580	151,256	-	(3,084,763)
Food service	445,582	147,370	302,496	-	4,284
Athletics	208,661	40,371	-	27,189	(141,101)
Transfers to other districts	131,416	-	-	-	(131,416)
Interest and costs on long-term debt	212,455	-	-	-	(212,455)
Unallocated depreciation	572,661	-	-	-	(572,661)
TOTAL EXPENSES	\$ 9,790,985	\$ 230,616	\$ 1,668,848	\$ 47,207	(7,844,314)
General Revenues					
Property taxes					2,425,311
State school aid - unrestricted					5,727,559
Investment earnings					77,558
Special Education county allocation					31,862
Miscellaneous					102,103
TOTAL GENERAL REVENUES					8,364,393
CHANGE IN NET ASSETS					520,079
Net assets, beginning of year					3,707,568
Prior period adjustment					(89,929)
Net assets, end of year					\$ 4,137,718

See accompanying notes to financial statements.

Montabella Community Schools

GOVERNMENTAL FUNDS BALANCE SHEET

June 30, 2006

	General	Site and Facilities Sinking	Nonmajor Governmental Funds	Total Governmental Funds
ASSETS				
Cash and cash equivalents	\$ 1,490,633	\$ 456,589	\$ 458,554	\$ 2,405,776
Accounts receivable	2,137	-	195	2,332
Due from other funds	108,101	-	-	108,101
Due from other governmental units	1,268,026	-	-	1,268,026
Inventories	-	-	9,751	9,751
Prepays	2,500	-	-	2,500
TOTAL ASSETS	\$ 2,871,397	\$ 456,589	\$ 468,500	\$ 3,796,486
LIABILITIES AND FUND BALANCES				
LIABILITIES				
Accrued payroll	\$ 371,974	\$ -	\$ -	\$ 371,974
Other accrued liabilities	270,291	-	-	270,291
Due to other funds	-	-	108,101	108,101
Short-term note payable	1,255,000	-	-	1,255,000
Due to other governmental units	324,919	-	2,892	327,811
TOTAL LIABILITIES	2,222,184	-0-	110,993	2,333,177
FUND BALANCES				
Reserved for				
Inventories and prepaids	2,500	-	9,751	12,251
Debt service	-	-	317,444	317,444
Unreserved				
Undesignated, reported in				
General fund	646,713	-	-	646,713
Special revenue funds	-	-	27,877	27,877
Capital projects funds	-	456,589	2,435	459,024
TOTAL FUND BALANCES	649,213	456,589	357,507	1,463,309
TOTAL LIABILITIES AND FUND BALANCES	\$ 2,871,397	\$ 456,589	\$ 468,500	\$ 3,796,486

See accompanying notes to financial statements.

Montabella Community Schools

RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET TO
THE STATEMENT OF NET ASSETS

June 30, 2006

Total fund balance - governmental funds \$ 1,463,309

Amounts reported for the governmental activities in the statement of net assets are different because:

Noncurrent assets used in governmental activities are not financial resources
and therefore are not reported as assets in the governmental funds.

The cost of capital assets is	\$ 19,079,494	
Accumulated depreciation is	<u>(6,361,889)</u>	12,717,605
Deferred charges, net of ammortization		105,922

Long-term liabilities are not due and payable in the current period
and therefore are not reported as liabilities in the funds.

Long-term liabilities at year-end consist of:

Deferred amounts on refunding	316,459	
Bonds, loans and capital leases payable	(10,331,040)	
Accrued interest payable	(84,979)	
Severance pay	<u>(49,558)</u>	<u>(10,149,118)</u>

Net assets of governmental activities \$ 4,137,718

See accompanying notes to financial statements.

Montabella Community Schools

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES -
GOVERNMENTAL FUNDS

Year Ended June 30, 2006

	General	Site and Facilities Sinking	Nonmajor Governmental Funds	Totals Governmental Funds
REVENUES				
Local sources	\$ 1,280,329	\$ 276,081	\$ 1,268,317	\$ 2,824,727
State sources	6,417,295	-	45,306	6,462,601
Federal sources	674,244	-	244,667	918,911
OTHER FINANCING SOURCES				
Bond proceeds	-	-	7,895,000	7,895,000
Bond premium	-	-	339,063	339,063
Transfers from other funds	-	-	143,648	143,648
Other transactions	104,825	-	-	104,825
TOTAL REVENUES AND OTHER FINANCING SOURCES	8,476,693	276,081	9,936,001	18,688,775
EXPENDITURES				
Current				
Instruction	4,951,308	-	-	4,951,308
Supporting services	3,242,413	-	-	3,242,413
Food service	-	-	445,582	445,582
Athletics	-	-	208,661	208,661
Debt service				
Principal retirement	5,000	-	530,692	535,692
Interest, fiscal and other charges	-	-	522,432	522,432
Capital outlay	-	235,975	1,183	237,158
OTHER FINANCING USES				
Transfers to other funds	143,648	-	-	143,648
Payments to escrow agent	-	-	8,265,575	8,265,575
Payments to other districts	131,416	-	-	131,416
TOTAL EXPENDITURES AND OTHER FINANCING USES	8,473,785	235,975	9,974,125	18,683,885
EXCESS OF REVENUES AND OTHER FINANCING SOURCES OVER (UNDER) EXPENDITURES AND OTHER FINANCING USES	2,908	40,106	(38,124)	4,890
Fund balances, beginning of year	736,234	416,483	395,631	1,548,348
Prior period adjustment	(89,929)	-	-	(89,929)
Fund balances, end of year	<u>\$ 649,213</u>	<u>\$ 456,589</u>	<u>\$ 357,507</u>	<u>\$ 1,463,309</u>

See accompanying notes to financial statements.

Montabella Community Schools

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN
FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES

Year Ended June 30, 2006

Net change in fund balances - total governmental funds \$ 4,890

Amounts reported for governmental activities in the statement of activities are different because:

Capital outlays are reported as expenditures in governmental funds. However, in the statement of activities, the cost of capital assets is allocated over their estimated useful lives as depreciation expense. In the current period, these amounts are:

Capital outlay	\$ 207,972	
Depreciation expense	<u>(572,661)</u>	
Excess of depreciation expense over capital outlay		(364,689)

Repayment of long-term debt and borrowing of long-term debt is reported as expenditures and other financing sources in governmental funds, but the repayment reduces long-term liabilities and the borrowings increase long-term liabilities in the statement of net assets. In the current year, these amounts consist of:

Net effect of long-term debt issuance and related items	8,222,381	
Bond and loan principal retirement	535,692	
Bond proceeds	<u>(7,895,000)</u>	
Excess of bond principal retirement over bond proceeds		863,073

Some items reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. These activities consist of:

Decrease in accrued interest payable	14,108	
Decrease in accrued severance pay	<u>2,697</u>	
		<u>16,805</u>

Change in net assets of governmental activities \$ 520,079

See accompanying notes to financial statements.

Montabella Community Schools

Fiduciary Funds

STATEMENT OF FIDUCIARY NET ASSETS

June 30, 2006

	Private Purpose Trust Fund	Agency Fund
ASSETS		
Cash	\$ 1,312	\$ 107,955
Investments	39,018	19,060
TOTAL ASSETS	40,330	<u>\$ 127,015</u>
LIABILITIES		
Due to individuals		
High School	-	\$ 69,455
Middle School	-	16,682
Webb Elementary	-	4,631
Blanchard Elementary	-	1,607
Preschool	-	30,987
Blanchard 5th Grade	-	3,653
TOTAL LIABILITIES	-0-	<u>\$ 127,015</u>
NET ASSETS		
Held in trust for private purposes	<u>\$ 40,330</u>	

See accompanying notes to financial statements.

Montabella Community Schools

Fiduciary Funds

STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS

Year Ended June 30, 2006

	Private Purpose Trust Fund
ADDITIONS	
Investment earnings	
Interest	\$ 760
Contributions	<u>10,000</u>
TOTAL ADDITIONS	10,760
DEDUCTIONS	
Other supporting services	<u>1,103</u>
CHANGE IN NET ASSETS	9,657
Net assets - beginning of year	<u>30,673</u>
Net assets - end of year	<u><u>\$ 40,330</u></u>

See accompanying notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

June 30, 2006

NOTE A: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of Montabella Community Schools have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The District's more significant accounting policies are described below.

1. Reporting Entity

As required by accounting principles generally accepted in the United States of America; GASB Statement No. 14, *The Financial Reporting Entity* (as amended by GASB Statement No. 39); and *Statement on Michigan Governmental Accounting and Auditing No. 5*, these financial statements present the financial activities of Montabella Community Schools (primary government). The District has no activities that would be classified as component units.

2. Basis of Presentation

DISTRICT-WIDE FINANCIAL STATEMENTS

The statement of net assets and the statement of activities (the district-wide statements) present information for the district as a whole. All non-fiduciary activities of the primary government are included (i.e., fiduciary fund activities are not included in the district-wide statements). Interfund activity has been eliminated in the preparation of the district-wide financial statements.

The district-wide and fiduciary fund financial statements are presented using the economic resources measurement focus, similar to that used by business enterprises or not-for-profit organizations. Because another measurement focus is used in the governmental fund financial statements, reconciliations are provided that explain the differences in detail.

The statement of activities presents the direct functional expenses of the District and the program revenues that support them. Direct expenses are specifically associated with a service, program, or department and are therefore clearly identifiable to a particular function. Program revenues are associated with specific functions and include charges to recipients of goods or services and grants and contributions that are restricted to meeting the operational or capital requirements of that function. Revenues that are not required to be presented as program revenues are general revenues. This includes all taxes, interest, and unrestricted State aid payments and other general revenues and shows how governmental functions are either self-financing or supported by the general revenues of the District.

FUND FINANCIAL STATEMENTS

The District uses funds to maintain its financial records during the year. A fund is defined as a fiscal and accounting entity with a self balancing set of accounts. The District utilizes governmental and fiduciary funds.

The governmental fund financial statements present the District's individual major funds and aggregated nonmajor funds. Separate columns are shown for the major funds on the balance sheet and statement of revenues, expenditures, and changes in fund balances. Nonmajor funds are combined and shown in a single column.

All governmental funds are presented using the current financial resources measurement focus. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet. Operating statements of these funds present increases (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in net current assets.

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2006

NOTE A: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

2. Basis of Presentation - continued

The major funds of the District are:

- a. General Fund - The General Fund is used to account for money or other resources provided to the District to support the educational programs and general operations of the District.
- b. Site and Facilities Sinking Fund - The Site and Facilities Sinking Fund is used to account for the construction and repair of the facilities of the District.

3. Measurement Focus

The government-wide and fiduciary private purpose trust fund financial statements are presented using the economic resources measurement focus, similar to that used by business enterprises or not-for-profit organizations. Because another measurement focus is used in the governmental fund financial statements, reconciliations to the government-wide statements are provided that explain the differences in detail.

All governmental funds are presented using the current financial resources measurement focus. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet. Operating statements of these funds present increases (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in net current assets.

There is no measurement focus for fiduciary agency fund since assets equal liabilities.

4. Basis of Accounting

Basis of accounting refers to the timing under which transactions are recognized for financial reporting purposes. Governmental fund financial statements use the modified accrual basis of accounting. The district-wide and fiduciary fund financial statements are prepared using the accrual basis of accounting.

Under the accrual basis of accounting, revenue is recorded in the period in which it is earned and expenses are recorded when incurred, regardless of the timing of related cash flows. Property tax revenue is recognized in the fiscal year for which it is levied. Revenues for grants, entitlements, and donations are recognized when all eligibility requirements imposed by the provider have been met. Deferred revenue is recorded when resources are received by the District before it has legal claim to them, such as when grant monies are received prior to the incurrence of qualified expenditures.

Under the modified accrual basis of accounting, revenues are recognized when susceptible to accrual (i.e., when they become both measurable and available). "Measurable" means the amount of the transaction can be determined and "available" means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Revenues susceptible to accrual include property taxes, state and federal aid, and interest revenue. Other revenues are not susceptible to accrual because generally they are not measurable until received in cash. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt which are recorded when due.

The District reports deferred revenue on its governmental funds balance sheet. Deferred revenues arise when potential revenue does not meet both the "measurable" and "available" criteria for recognition in the current period. Resources are considered available if they are collected during the current fiscal year or soon enough afterward to be used in payment of current year liabilities - defined as expected to be received within sixty days of year-end. Deferred revenues also arise when the District receives resources before it has a legal claim to them. In subsequent periods, when both revenue recognition criteria are met, the liability for deferred revenue is removed from the balance sheet and revenue is recognized.

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2006

NOTE A: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

5. Budgets and Budgetary Accounting

Budgets are adopted on a basis consistent with accounting principles generally accepted in the United States of America. Annual appropriated budgets are adopted for the General and Special Revenue funds. All unexpended appropriations lapse at fiscal year-end.

The District follows these procedures in establishing the budgetary data reflected in the financial statements:

- a. The Superintendent submits to the School Board a proposed operating budget for the fiscal year commencing on July 1. The operating budget includes proposed expenditures and the means for financing them.
- b. Public hearings are conducted to obtain taxpayer comments.
- c. Prior to July 1, the budget is legally adopted by School Board resolution pursuant to the Uniform Budgeting and Accounting Act (P.A. 621 of 1978). The Act requires that the budget be amended prior to the end of the fiscal year when necessary to adjust appropriations if it appears that revenues and other financing sources will not be in excess of original estimates. Expenditures shall not be made or incurred, unless authorized in the budget, in excess of the amounts appropriated.
- d. The budgets are legally adopted at the functional level; however, they are maintained at the object level for control purposes. Any revisions that alter the total expenditures at the functional level by more than \$1,500 must be approved by the School Board.
- e. Formal budgetary integration is employed as a management control device during the year for the General and Special Revenue Funds.
- f. The budgets, as presented, have been amended in a legally permissible manner. Supplemental appropriations were made during the year with the last one approved June 26, 2006.

6. Cash, Cash Equivalents, and Investments

Cash and cash equivalents consist of checking, savings, money market accounts, pooled investment funds, and certificates of deposit with an original maturity of 90 days or less. Cash equivalents are recorded at cost, which approximates market value.

Investments consist of certificates of deposit with an original maturity of greater than 90 days. Certificates of deposit are recorded at cost, which approximates market value.

7. Short-term Interfund Receivables/Payables

During the course of operations, numerous transactions occur between individual funds for goods provided or services rendered. These receivables and payables are classified as "due from other funds" and "due to other funds" on the balance sheet.

8. Due From Other Governmental Units

Due from other governmental units consists of various amounts owed to the District for grant programs and State Aid payments. The total amount of \$1,268,026 due from other governmental units consists of \$1,172,578 and \$95,448 related to State Aid and grant programs, respectively.

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2006

NOTE A: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

9. Inventories

Inventories are stated at cost on a first in/first out basis. The Food Services Fund inventory consists of food and paper goods. Inventory amounts are equally offset by a fund balance reserve which indicates that they do not constitute "available spendable resources" even though they are a component of net current assets.

10. Capital Assets

Capital assets include land, buildings, equipment, and vehicles and are recorded (net of accumulated depreciation, if applicable) in the district-wide financial statements. Capital assets are those with an initial individual cost greater than \$5,000 and an estimated useful life of more than one year, except for new computers, printers, data projectors and televisions (which have no cost threshold) and all new classrooms (recorded at total content cost). Capital assets are not recorded in the governmental funds. Instead, capital acquisition and construction are reflected as expenditures in governmental funds. All purchased capital assets are valued at cost where historical records are available and at an estimated historical cost where no historical records exist. Donated capital assets are valued at their estimated fair market value on the date received.

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized. Depreciation is computed using the straight-line method over the following useful lives:

Buildings and improvements	20 - 50 years
Equipment	5 - 20 years
Vehicles	8 years

The District has no assets that would be classified as infrastructure assets.

11. Compensated Absences

Based on the requirements of GASB Statement No. 16, *Accounting for Compensated Absences*, the District has recorded all liabilities associated with compensated absences. Accumulated vested severance amounts and nonvested severance amounts that are probable to vest and be paid at termination are considered payable from future resources and are recorded along with the related payroll taxes as a long-term liability in the district-wide financial statements.

12. Accrued Interest Payable

Accrued interest is presented for long-term obligations in the district-wide statements in two components: the portion of accrued interest payable that is due within one year is reported as a current liability, the remaining amount that is not due within one year has been reported as a noncurrent liability. The interest payable on the Durant Resolution bonds that were due May 15, 2003 through May 15, 2005 is shown as a noncurrent liability due to the State of Michigan deferring the payments during this time period until May 15, 2011.

13. Short-Term Note Obligations

Short-term debt is recognized as a liability of a governmental fund and is included on the balance sheet of the applicable fund. During the current year the District borrowed funds to meet short-term cash flow borrowing needs. The final payment is due and payable in August 2006, and anticipated State Aid is expected to be sufficient to cover this commitment.

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2006

NOTE A: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

14. Long-term Obligations

Long-term debt is recognized as a liability in the district-wide statements when incurred. The portion of those liabilities expected to be paid within the next year is a current liability with the remaining amounts shown as long-term.

Long-term debt is recognized as a liability of a governmental fund when due or when resources have been accumulated in the Debt Service Fund for payment early in the following year. For other long-term obligations, only that portion expected to be financed from expendable available financial resources is reported as a fund liability of a governmental fund.

15. Property Taxes

Property taxes levied by the District are collected by various municipalities and periodically remitted to the District. The taxes are levied as of December 1 and are due upon receipt of the billing by the taxpayer. The actual due date is February 14, after which time the bills become delinquent and penalties and interest may be assessed by the collecting entity. School District property tax revenues are recognized when levied to the extent that they result in current revenue (collected as of year-end). Amounts received subsequent to June 30 are recognized as revenue when collected.

The District levied taxes of \$17.9784 per \$1,000 of taxable valuation on nonhomestead property for general governmental services, and \$1.8300 for 1999 Refunding Debt, \$3.6700 for 1999 Building and Site Bonds, and \$1.4982 for a building and site sinking fund per \$1,000 of taxable valuation on the total applicable taxable valuation of all property within the District.

16. State Foundation Revenue

Beginning with the fiscal year ended June 30, 1995, the State of Michigan adopted a foundation grant approach, which provides for a specific annual amount of revenue per student based on a statewide formula. Prior to the fiscal year ended June 30, 1995, the State utilized a district power equalizing approach. The foundation is funded from State and local sources. Revenues from State sources are primarily governed by the School Aid Act and the School Code of Michigan. The Michigan Department of Education administers the allocation of State funds to school districts based on information supplied by the districts. For the year ended June 30, 2006, the foundation allowance was based on the average of pupil membership counts taken in September 2005 and February 2005. The average calculation was weighted 75% for the September 2005 count and 25% for the February 2005 count.

The State portion of the foundation is provided primarily by a State education property tax millage of 6 mills and an allocated portion of State sales and other taxes. The local portion of the foundation is funded primarily by nonhomestead property taxes, which may be levied at a rate of up to 18 mills. The State revenue is recognized during the foundation period (currently the fiscal year) and is funded through nine (9) payments made during the year and two (2) payments made subsequent to year-end. The local revenue is recognized as outlined above under Property Taxes.

17. State Categorical Revenue

The District also receives revenue from the State to administer certain categorical education programs. State rules require that revenue earmarked for these programs be expended for its specific purpose. Categorical funds received which are not expended by the close of the fiscal year are reported as deferred revenue.

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2006

NOTE A: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

18. Interfund Transactions

Interfund transactions are reported as either loans, services provided, reimbursements or transfers. Loans are reported as interfund receivables and payables as appropriate and are subject to elimination upon consolidation. Services provided, deemed to be at market or near market rates, are treated as revenues and expenditures/expenses. Reimbursements are recorded when one fund incurs a cost, charges the appropriate benefiting fund and reduces its related cost as a reimbursement. All other interfund transactions are treated as transfers on the governmental fund financial statements. Transfers are netted as part of the reconciliation to the district-wide financial statements.

19. Comparative Data

Comparative data for the prior year has not been presented in the financial statements since their inclusion would make the statements unduly complex and difficult to read.

20. Federal Programs

Federal programs are accounted for in the General Fund and specific Special Revenue Funds. The District has not integrated its Single Audit reports and financial data as part of the financial statements. The Single Audit reports and financial data will be issued under separate cover as supplementary information to the financial statements.

NOTE B: CASH, CASH EQUIVALENTS, AND INVESTMENTS

In accordance with Michigan Public Act 451 of 1976, Section 1223(1), as amended, the District is authorized to invest its surplus funds in the following types of investments:

1. Bonds, bills, or notes of the United States; obligations, the principal and interest of which are fully guaranteed by the United States; or obligations of the State.
2. Certificates of deposit issued by a state or national bank, savings accounts of a state or federal savings and loan association, or certificates of deposit or share certificates of a state or federal credit union organized and authorized to operate in this state.
3. Commercial paper rated prime at the time of purchase and maturing not more than 270 days after the date of purchase.
4. Securities issued or guaranteed by agencies or instrumentalities of the United States government.
5. United States government or federal agency obligation repurchase agreements.
6. Bankers' acceptances issued by a bank that is a member of the Federal Depository Insurance Corporation.
7. Mutual funds composed entirely of investment vehicles that are legal for direct investment by a School District.
8. Investment pools, as authorized by the Surplus Funds Investment Pool Act, Act No. 367 of the Public Acts of 1982, being sections 129.111 to 129.118 of the Michigan Compiled Laws, composed entirely of instruments that are legal for direct investment by a School District.

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2006

NOTE B: CASH, CASH EQUIVALENTS, AND INVESTMENTS - CONTINUED

Michigan Public Acts authorize school districts in Michigan to deposit in the accounts of federally insured banks, credit unions, and savings and loan associations. Deposits of the District are at federally insured banks and credit unions in the State of Michigan in the name of the School District.

Federal Deposit insurance Corporation (FDIC), Federal Savings and Loan Insurance Corporation (FSLIC) and the National Credit Union Administration regulations provide that deposits of governmental units are to be separately insured for savings deposits and demand deposits up to \$100,000 each. Furthermore, if specific deposits are regulated by statute or bond indenture, these specific deposits are to be separately insured for the amount of \$100,000. Michigan School Code Section 1223 allows that security in the form of collateral, surety bond, or another form may be taken for the deposits or investments of a school district in a bank, savings and loan association, or credit union.

Deposits

There is a custodial credit risk as it relates to deposits. In the case of deposits, this is the risk that in the event of a bank failure, the District's deposits may not be returned to it. As of June 30, 2006, the carrying amount of the District's deposits was \$966,352 and the bank balance was \$1,411,862 of which \$259,390 was covered by federal depository insurance. The balance of \$1,152,472 was uninsured and uncollateralized. The District had \$100 of imprest cash on hand.

Investments

As of June 30, 2006, the District had the following investments:

<u>Investment type</u>	<u>Fair value</u>	<u>Bank Balance</u>	<u>Weighted Average Maturity</u>
Insured or registered for which the securities are held by the District's name			
Mutual Funds - Government Fund	\$ 14,342	\$ 14,342	30 days
Uncategorized pooled investments	<u>1,592,327</u>	<u>1,592,327</u>	< 12 months average
	<u>\$ 1,606,669</u>	<u>\$ 1,606,669</u>	

Credit risk

State law limits investments in certain types of investments to a prime or better rating issued by nationally recognized statistical rating organizations (NRSRO's). As of June 30, 2006, the District's investments in the Government Fund and the uncategorized pooled investment (the Michigan Liquid Asset Fund Plus) were rated AAAM and AAA by Standard and Poor's, respectively.

Interest rate risk

The district has not adopted a policy that indicates how the District will minimize interest rate risk, which is the risk that the market value of securities in the portfolio will fall due to changes in market interest rates.

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2006

NOTE B: CASH, CASH EQUIVALENTS, AND INVESTMENTS - CONTINUED

Concentration of credit risk

The District has not adopted a policy that indicates how the District will minimize concentration of credit risk, which is the risk of loss attributed to the magnitude of the District's investment in a single issuer.

Custodial credit risk

The District has not adopted a policy that indicates how the District will minimize custodial credit risk, which is the risk that in the event of the failure of the counterparty, the District will not be able to recover the value of its investments of collateral securities that are in possession of an outside party.

As of June 30, 2006, the cash and cash equivalents and investments referred to above have been reported in either the cash and cash equivalents or investments captions in the basic financial statements in the following categories:

	<u>Governmental Activities</u>	<u>Fiduciary Funds</u>	<u>Total Primary Government</u>
Cash and cash equivalents	\$ 2,405,776	\$ 109,267	\$ 2,515,043
Investments	<u>-</u>	<u>58,078</u>	<u>58,078</u>
	<u>\$ 2,405,776</u>	<u>\$ 167,345</u>	<u>\$ 2,573,121</u>

Due to significantly higher cash flow at certain periods during the year, the amount the District held as cash, cash equivalents and investments increased significantly. As a result, the amount of uninsured and uncollateralized cash, cash equivalents, and investments were substantially higher at these peak periods than at year-end.

NOTE C: CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2006 was as follows:

	<u>Balance July 1, 2005</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance June 30, 2006</u>
Vehicles	\$ 68,089	\$ -	\$(301)	\$ 67,788
Buildings and improvements	16,529,039	187,550	-	16,716,589
Equipment	<u>2,274,695</u>	<u>20,422</u>	<u>-</u>	<u>2,295,117</u>
Subtotal	18,871,823	207,972	(301)	19,079,494
Less accumulated depreciation for:				
Vehicles	(42,986)	(3,812)	301	(46,497)
Buildings and improvements	(4,571,373)	(373,222)	-	(4,944,595)
Equipment	<u>(1,175,170)</u>	<u>(195,627)</u>	<u>-</u>	<u>(1,370,797)</u>
Subtotal	<u>(5,789,529)</u>	<u>(572,661)</u>	<u>301</u>	<u>(6,361,889)</u>
Capital assets, net	<u>\$ 13,082,294</u>	<u>\$(364,689)</u>	<u>\$ -0-</u>	<u>\$ 12,717,605</u>

Depreciation expense was not allocated to governmental functions. It appears on the statement of activities as "unallocated".

Montabella Community Schools

NOTES TO FINANCIAL STATEMENTS

June 30, 2006

NOTE D: LONG-TERM DEBT

The following is a summary of changes in long-term debt obligations of the District for the year ended June 30, 2006.

	Balance July 1, 2005	Additions	Deletions	Balance June 30, 2006	Amounts Due Within One Year
General Long-Term Debt					
1999 Refunding Bonds	\$ 665,000	\$ -	\$ 325,000	\$ 340,000	\$ 340,000
1998 Durant Resolution Bonds	75,127	-	5,692	69,435	5,962
1999 School Building and Site	10,025,000	-	8,000,000	2,025,000	210,000
2005 Refunding Bonds	-	7,895,000	-	7,895,000	25,000
Other Notes and Loans	6,605	-	5,000	1,605	1,605
Severance Pay	<u>52,255</u>	<u>-</u>	<u>2,697</u>	<u>49,558</u>	<u>12,389</u>
	10,823,987	7,895,000	8,338,389	10,380,598	594,956
Less deferred amounts on refunding	<u>-</u>	<u>339,063</u>	<u>22,604</u>	<u>316,459</u>	<u>22,604</u>
	<u>\$10,823,987</u>	<u>\$ 7,555,937</u>	<u>\$ 8,315,785</u>	<u>\$10,064,139</u>	<u>\$ 572,352</u>

Significant details regarding outstanding long-term debt (including current portions) are presented below:

General Obligation Bonds

\$2,460,000 1999 Refunding Bonds dated February 22, 1999, due in an annual installment of \$340,000, with interest of 4.0 percent, payable semi-annually.	\$ 340,000
\$10,550,000 1999 Building and Site Bonds dated August 1, 1999, due in annual installments ranging from \$210,000 to \$635,000, with interest of 4.85 percent, payable semi-annually.	2,025,000
\$7,895,000 2005 Refunding Bonds dated July 14, 2005, due in annual installments ranging from \$25,000 to \$805,000, with interest ranging from 3.0 to 4.75 percent, payable semi-annually.	<u>7,895,000</u>
	<u>\$10,260,000</u>

Resolution Bonds

\$117,596 1998 Durant Resolution Bonds dated November 15, 1998, due in annual installments ranging from \$5,962 to \$28,421 including interest of 4.7615353 percent, payable annually. The annual debt service payments related to these bonds is paid through an annual appropriation from the State of Michigan.	<u>\$ 69,435</u>
--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------	------------------

Other Notes and Loans

\$89,374 U.S. Environmental Protection Agency Promissory Note dated April 6, 1987, due in one final principal installment of \$1,605.	<u>\$ 1,605</u>
---------------------------------------------------------------------------------------------------------------------------------------	-----------------

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2006

NOTE D: LONG-TERM DEBT - CONTINUED

Advance Refunding - Current

On July 14, 2005 the District defeased the portion of the 1999 School Building and Site Bonds, which are due and payable May 1, 2011 through May 1, 2020. This was accomplished by establishing an irrevocable trust with an escrow agent composed of cash and U.S. government securities sufficient to meet the applicable principal and interest obligations. The District issued General Obligation 2005 Refunding Bonds in the amount of \$7,895,000 to provide resources to fund the escrow amounts and pay the costs of issuance of the refunding bonds. Accordingly, the trust account assets and liabilities for the defeased bonds are not included in the District's financial statements. At June 30, 2006, bonds due and payable May 1, 2011 through May 1, 2020 for the 1999 School Building and Site Bonds in the amount of \$7,800,000 are considered defeased.

As a result of the advance refunding, the District decreased its total debt service requirements by \$607,573, which resulted in an economic gain (difference between the present value of the debt service payments on the old and new debt) of \$444,737.

Severance Pay

In recognition of services to the District, a severance payment will be made upon termination to eligible employees according to their respective employment contracts or past District practice as follows:

Teachers and Administrative Staff

Employees with at least fifteen (15) years of service will be paid up to fifty (50) days of accumulated sick days at a rate of \$15 per day.

Support Staff

Employees with at least ten (10) years of service will be paid up to fifty (50) days of accumulated sick days at a rate of \$15 per day.

Under GASB Statement No. 16 requirements, the District has elected to implement the "vesting" method of calculating the compensated absences liability. The amounts accumulated for all employees currently vested are calculated along with an amount for other employees who currently are not vested but are probable to vest in future years. The amounts for employees who currently are not vested are calculated taking total unused sick amounts at June 30, 2006, for all non-vested employees and multiplying it by a historical termination percentage. This percentage is based on an estimate of the percentage of employees who have terminated employment fully vested in the past five (5) years.

A summary of the calculated amounts of accrued severance pay and related payroll taxes as of June 30, 2006, which has been recorded in the District-wide financial statements, is as follows:

	<u>Vested Employees</u>	<u>Non-vested Employees</u>	<u>Total</u>
Severance pay	\$ 27,409	\$ 18,627	\$ 46,036
Payroll taxes	<u>2,097</u>	<u>1,425</u>	<u>3,522</u>
	<u>\$ 29,506</u>	<u>\$ 20,052</u>	<u>\$ 49,558</u>

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2006

NOTE D: LONG-TERM DEBT - CONTINUED

The annual requirements to pay the debt principal and interest outstanding for the Long-Term Debt are as follows:

Year Ending June 30,	<u>Durant Resolution Bonds</u>		<u>2005 Refunding Bonds</u>		<u>1999 Building and Site Bonds</u>	
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>
2007	\$ 5,962	\$ 2,295	\$ 25,000	\$ 339,498	\$ 210,000	\$ 98,213
2008	6,247	2,011	25,000	338,748	575,000	88,028
2009	6,545	1,714	25,000	337,998	605,000	60,140
2010	6,856	1,402	25,000	337,248	635,000	30,798
2011	28,421	10,549	695,000	336,473	-	-
2012-2016	15,404	1,109	3,880,000	1,187,225	-	-
2017-2020	-	-	3,220,000	319,988	-	-
	<u>\$ 69,435</u>	<u>\$ 19,080</u>	<u>\$ 7,895,000</u>	<u>\$ 3,197,178</u>	<u>\$ 2,025,000</u>	<u>\$ 277,179</u>

Year Ending June 30,	<u>1999 Refunding Bonds</u>		<u>Other Notes and Loans</u>	
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>
2007	\$ 340,000	\$ 13,600	\$ 1,605	\$ -
2008	-	-	-	-
2009	-	-	-	-
2010	-	-	-	-
2011	-	-	-	-
2012-2016	-	-	-	-
2017-2020	-	-	-	-
	<u>\$ 340,000</u>	<u>\$ 13,600</u>	<u>\$ 1,605</u>	<u>\$ -0-</u>

The Durant Resolution Bonds referred to above are bonds whose future debt service payments by the District are contingent on an annual State of Michigan appropriation. This is the only revenue source for making the annual debt service payments on these bonds. If the legislature of the State of Michigan fails to appropriate the funds, in any particular year, the District is under no obligation for payment of that year's debt obligation.

NOTE E: INTERFUND RECEIVABLES AND PAYABLES

The amount of interfund receivables and payables at June 30, 2006, are as follows:

Due to General Fund from:
Nonmajor governmental funds \$ 108,101

Amounts appearing as interfund payables and receivables arise from two types of transactions. One type of transaction is where a fund will pay for a good or service that at least a portion of the benefit belongs to another fund. The second type of transaction is where one fund provides a good or service to another fund. Balances at the end of the year are for transfers that have not cleared as of the balance sheet date.

NOTE F: INTERFUND TRANSFERS

Permanent reallocation of resources between funds of the reporting entity is classified as interfund transfers. For the purpose of the statement of activities, all interfund transfers between individual governmental funds have been eliminated.

Transfers to nonmajor governmental funds from:
General Fund \$ 143,648

Montabella Community Schools

NOTES TO FINANCIAL STATEMENTS

June 30, 2006

NOTE G: EMPLOYEE RETIREMENT SYSTEM

All of the District's employees, except students, are eligible to participate in the statewide Michigan Public School Employees' Retirement System (MPERS), a multiple-employer, cost-sharing, statewide public employee retirement system. The MPERS issues a publicly available financial report that includes financial statements and required supplementary information for the Plan. The report for the fiscal year-end September 30, 2005, the last year available, may be obtained by contacting the State of Michigan Department of Management and Budget.

The payroll for employees covered by the MPERS for the year ended June 30, 2006, was \$4,691,403 of which \$3,035,576 was for members who have elected the MIP option; the District's total payroll was \$4,776,149.

Effective January 1, 1987, Act 91 of the Public Acts of 1985 established a voluntary contribution to the Member Investment Plan (MIP). Employees first hired before January 1, 1990, made a one-time irrevocable election to contribute to the tax deferred MIP. For a limited period ended January 1, 1993, an active Basic Plan member may have enrolled in MIP by repaying the contributions and interest that would have been made had MIP enrollment occurred initially prior to January 1, 1990. Employees first hired on or after January 1, 1990, will automatically be included in MIP.

Members in MIP may retire at any age after attaining thirty years of credited service, or at age sixty while still working with a minimum total of five years of credited service, with credited service in each of the five school fiscal years immediately preceding the retirement allowance effective date. The retirement allowance is calculated using a formula of 1.5% of the member's final average compensation multiplied by the total number of years of credited service.

Employees who did not elect the MIP option fall under the MPERS Basic Plan and may retire after attaining age sixty with ten or more years of credited service; or attaining age fifty-five with thirty or more years of credited service; or attaining age fifty-five while still working with at least fifteen but fewer than thirty years of credited service in each of the five school fiscal years immediately preceding the retirement allowance effective date. The retirement allowance is computed using a formula of 1.5% of the average of the highest total earnings during a period of sixty consecutive months (five years) multiplied by the total years to the nearest tenth of a year of credited service.

The MPERS also provides death and disability benefits and health and medical, dental, vision and hearing insurance coverage. Benefits are established by state statute.

Employees who selected MIP on or before December 31, 1989, contributed 4% from January 1, 1987, to December 31, 1989, and 3.9% thereafter. Employees first hired on or after January 1, 1990, are required to contribute based on a graduated rate: 3% of the first \$5,000; 3.6% of \$5,001 through \$15,000; 4.3% of all wages over \$15,000.

For the period of July 1, 2005 to September 30, 2005, the District is required by State statute to contribute 14.87% of covered compensation for all wages to the Plan. For the period of October 1, 2005 to June 30, 2006 the District is required by State statute to contribute 16.34% of covered compensation for all wages to the Plan.

The total amount contributed to the Plan for the year ended June 30, 2006, and the previous two (2) years is as follows:

<u>June 30,</u>	<u>MIP</u> <u>Contributions</u>	<u>District</u> <u>Contributions</u>	<u>Total</u> <u>Contributions</u>
2006	\$ 117,022	\$ 752,503	\$ 869,525
2005	105,614	644,872	750,486
2004	110,450	599,275	709,725

Montabella Community Schools

NOTES TO FINANCIAL STATEMENTS

June 30, 2006

NOTE G: EMPLOYEE RETIREMENT SYSTEM - CONTINUED

The following represents contributions as a percentage of the applicable covered payroll for the current and preceding two (2) years:

<u>June 30,</u>	<u>MIP</u> <u>Contributions</u>	<u>District</u> <u>Contributions</u>
2006	3.8 %	16.0 %
2005	3.8	14.4
2004	3.8	13.0

NOTE H: FUND BALANCE RESERVES

Reserved fund balance is used to earmark a portion of fund balance to indicate that it is not appropriate for expenditures or has been legally segregated for a specific future use.

The following are the various fund balance reserves as of June 30, 2006:

General Fund	
Reserved for prepaids	\$ <u>2,500</u>
Nonmajor governmental funds	
Reserved for inventories	\$ 9,751
Reserved for debt service	<u>317,444</u>
	<u>\$ 327,195</u>

NOTE I: EXCESS OF EXPENDITURES OVER APPROPRIATIONS

Michigan Public Act 621 of 1978, Section 18 and 19, as amended, provides that a local governmental unit not incur expenditures in excess of the amounts appropriated.

In the body of the budgetary comparison schedule, the District's budgeted expenditures in the General Fund have been adopted and shown at the functional classification level. Budgeted expenditures for nonmajor Special Revenue funds have not been presented.

During the year ended June 30, 2006, the District incurred expenditures in excess of the amounts appropriated as follows:

	<u>Amounts</u> <u>Appropriated</u>	<u>Amounts</u> <u>Expended</u>	<u>Variance</u>
General Fund			
Basic programs			
Preschool	\$ 127,429	\$ 129,772	\$ 2,343
Added needs			
At-risk	124,190	124,259	69
Other financing uses			
Transfers to other funds	134,400	143,648	9,248

Montabella Community Schools

NOTES TO FINANCIAL STATEMENTS

June 30, 2006

NOTE J: FLEXIBLE BENEFITS PLAN

In October 1996 the District approved by Board action to implement a flexible benefits cafeteria plan established under Section 125 of the Internal Revenue Code. The Plan, available to all employees, permits them to receive cash in lieu of medical benefits. The Plan, effective October 1, 1997, provides employees with the opportunity to choose among benefits consisting of cash or health benefits.

The Plan is administered by Montabella Community Schools.

NOTE K: RISK MANAGEMENT

The District participates in a pool, the MASB-SEG Property and Casualty Pool with other school districts for property, liability, and errors and omissions. The pool is organized under Public Act 138 of 1982, as amended as a governmental group property and casualty self insurance pool. The District has no liability for additional assessments based on the claims filed against the pool nor do they have rights to dividends.

The District also participates in a pool, the SEG Self-Insured Workers' Disability Compensation Fund, with other school districts for workers' compensation losses. The pool is organized under Public Act 317 of 1969, as amended. The District has no liability for additional assessments based on the claims filed against the pool nor do they have any rights to dividends.

NOTE L: SPECIAL EDUCATION UNDERFUNDING SETTLEMENT

Prior to the current year the Durant vs. State of Michigan case was settled and the State was required to reimburse each plaintiff and nonplaintiff an agreed upon amount for past underfunding of special education. Montabella Community Schools, a nonplaintiff District, was awarded \$235,193 in the settlement. These funds are being paid as follows:

- a. One-half is being paid over the next ten (10) years, which began November 15, 1998. The restrictions on use of these funds are detailed within State School Aid Act, Section 11F(6). These funds are recorded within the General Fund as categorical State Aid. At the end of the current year all these funds had been expended.
- b. One-half is being paid over the next fifteen (15) years, which began May 15, 1999. The District borrowed this portion of the settlement amount through the Michigan Municipal Bond Authority on November 15, 1998. These funds were recorded as bond proceeds in the Capital Projects Fund. The bond proceeds may be used for any purpose specified in Section 1351 (a) of the Revised School Code. The debt service payments or these bonds are to be made through an annual legislative appropriation. If the State of Michigan legislature fails to make the annual appropriation the District is under no obligation for the debt Payments for that year. The District has pledged the annual State payments to the Michigan Municipal Bond Authority for payment of debt service.

NOTE M: BONDED CONSTRUCTION AND SINKING FUNDS

The Capital Projects Funds of the District include the capital project activities funded by the Middle School Construction Bonds and from local millage for a bond sinking fund. For the expenditures recorded within the Middle School Capital Project Fund, the District has complied with the applicable provisions of Section 1351 (a) of the Revised School Code. For the expenditures recorded within the Site and Facilities Sinking Fund, the District has complied with the applicable provisions of Section 1212 (1) of the Revised School Code and the Michigan Department of Treasury Letter No. 01-95.

Montabella Community Schools
NOTES TO FINANCIAL STATEMENTS

June 30, 2006

NOTE N: SHORT-TERM NOTES

On August 19, 2005, the District issued a short-term State School Aid Anticipation Note in the amount of \$1,255,000 for the purpose of funding operating expenditures until the 2006 State Aid payments resumed. This short-term note, which has a net outstanding balance of \$1,255,000 at June 30, 2006, is reported in the General Fund under the caption short-term notes payable. The outstanding balance is due August 18, 2006.

NOTE O: RESTRICTED NET ASSETS

Restrictions of net assets shown in the District-wide financial statements indicate that restrictions imposed by the funding source or some other outside source which precludes their use for unrestricted purposes. The following is the net asset restriction as of June 30, 2006:

Governmental activities	
Restricted for debt service	\$ 232,465
Restricted for sinking fund activities	<u>456,589</u>
	<u>\$ 689,054</u>

NOTE P: PRIOR PERIOD ADJUSTMENTS

The following prior period adjustments were made during the year, which were the result of the correction of accounting errors. These adjustment were reported as a change to beginning fund balance and beginning net assets. The effect on operations and other affected balances for the current year are as follows:

	June 30, <u>2006</u>	<u>2005</u>	<u>Description</u>
General Fund			
Due to State	\$ -	\$ 89,929	Correct understatement of due to State
Revenue over (under) expenditures	-	(89,929)	
Fund balance - beginning	(89,929)	-	
Governmental Activities			
Due to State	-	89,929	Correct understatement of due to State
Change in net assets	-	(89,929)	
Net assets – beginning	(89,929)	-	

REQUIRED SUPPLEMENTARY INFORMATION

Montabella Community Schools

General Fund

BUDGETARY COMPARISON SCHEDULE

Year Ended June 30, 2006

	Original Budget	Final Amended Budget	Actual	Variance with Final Budget Positive (Negative)
REVENUES				
Local sources	\$ 1,378,389	\$ 1,256,284	\$ 1,280,329	\$ 24,045
State sources	6,331,631	6,386,958	6,417,295	30,337
Federal sources	665,293	653,270	674,244	20,974
OTHER FINANCING SOURCES				
Other transactions	150,750	107,726	104,825	(2,901)
TOTAL REVENUES AND OTHER FINANCING SOURCES	8,526,063	8,404,238	8,476,693	72,455
EXPENDITURES				
INSTRUCTION				
Basic programs				
Preschool	130,993	127,429	129,772	(2,343)
Elementary	1,383,997	1,345,083	1,330,405	14,678
Middle school	1,198,583	1,231,178	1,220,451	10,727
High School	1,203,214	1,179,381	1,167,624	11,757
Alternative education	71,874	74,417	62,010	12,407
Total basic programs	3,988,661	3,957,488	3,910,262	47,226
Added needs				
At-risk	152,809	124,190	124,259	(69)
Special education	449,543	443,366	441,902	1,464
Compensatory education	455,651	460,496	451,000	9,496
Vocational education	23,950	24,693	23,885	808
Total added needs	1,081,953	1,052,745	1,041,046	11,699
TOTAL INSTRUCTION	5,070,614	5,010,233	4,951,308	58,925
SUPPORTING SERVICES				
Pupil	365,578	405,231	396,199	9,032
Instructional staff	449,097	472,558	451,472	21,086
General administration	205,659	188,937	179,617	9,320
School administration	480,160	458,546	443,667	14,879
Business services	227,609	243,248	241,375	1,873
Central services	135,111	165,497	151,455	14,042
Pupil transportation	633,944	659,023	652,750	6,273
Operation and maintenance	758,455	735,314	716,895	18,419
Other	7,275	8,400	8,983	(583)
TOTAL SUPPORTING SERVICES	3,262,888	3,336,754	3,242,413	94,341

Montabella Community Schools

General Fund

BUDGETARY COMPARISON SCHEDULE - CONTINUED

Year Ended June 30, 2006

	Original Budget	Final Amended Budget	Actual	Variance with Final Budget Positive (Negative)
DEBT SERVICE				
Principal	\$ 5,000	\$ 5,000	\$ 5,000	\$ -0-
OTHER FINANCING USES				
Transfers to other funds	128,400	134,400	143,648	(9,248)
Payments to other districts	112,479	153,400	131,416	21,984
TOTAL OTHER FINANCING USES	240,879	287,800	275,064	12,736
TOTAL EXPENDITURES AND OTHER FINANCING USES	8,579,381	8,639,787	8,473,785	166,002
EXCESS OF REVENUES AND OTHER FINANCING SOURCES OVER (UNDER) EXPENDITURES AND OTHER FINANCING USES	(53,318)	(235,549)	2,908	238,457
Fund balance, beginning of year	736,234	736,234	736,234	-0-
Prior period adjustment	-	-	(89,929)	(89,929)
Fund balance, end of year	\$ 682,916	\$ 500,685	\$ 649,213	\$ 148,528

OTHER SUPPLEMENTARY INFORMATION

Montabella Community Schools

Nonmajor Governmental Funds

COMBINING BALANCE SHEET

June 30, 2006

	Special Revenue Funds		Debt
	Food Service	Athletics	1999 Refunding Bonds
ASSETS			
Cash and cash equivalents	\$ 119,218	\$ 14,981	\$ 61,016
Accounts receivable	-	195	-
Inventories	9,751	-	-
TOTAL ASSETS	\$ 128,969	\$ 15,176	\$ 61,016
LIABILITIES AND FUND BALANCES			
LIABILITIES			
Due to other funds	\$ 106,517	\$ -	\$ 1,584
Due to other governmental units	-	-	2,892
TOTAL LIABILITIES	106,517	-0-	4,476
FUND BALANCES			
Reserved for			
Inventories	9,751	-	-
Debt service	-	-	56,540
Unreserved			
Undesignated, reported in:			
Special revenue funds	12,701	15,176	-
Capital projects funds	-	-	-
TOTAL FUND BALANCES	22,452	15,176	56,540
TOTAL LIABILITIES AND FUND BALANCES	\$ 128,969	\$ 15,176	\$ 61,016

Service Funds		Capital Projects Fund	Total Nonmajor Governmental Funds
Middle School Debt	Durant Bonds	Middle School	
\$ 260,904	\$ -	\$ 2,435	\$ 458,554
-	-	-	195
-	-	-	9,751
<u>\$ 260,904</u>	<u>\$ -0-</u>	<u>\$ 2,435</u>	<u>\$ 468,500</u>
\$ -	\$ -	\$ -	\$ 108,101
-	-	-	2,892
-0-	-0-	-0-	110,993
-	-	-	9,751
260,904	-	-	317,444
-	-	-	27,877
-	-	2,435	2,435
<u>260,904</u>	<u>-0-</u>	<u>2,435</u>	<u>357,507</u>
<u>\$ 260,904</u>	<u>\$ -0-</u>	<u>\$ 2,435</u>	<u>\$ 468,500</u>

Montabella Community Schools

Nonmajor Governmental Funds

COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN
FUND BALANCES

Year Ended June 30, 2006

	Special Revenue Funds		Debt 1999 Refunding Bonds
	Food Service	Athletics	
REVENUES			
Local sources	\$ 170,861	\$ 74,759	\$ 350,411
State sources	37,048	-	-
Federal sources	244,667	-	-
OTHER FINANCING SOURCES			
Bond proceeds	-	-	-
Bond premium	-	-	-
Transfers from other funds	-	143,648	-
TOTAL REVENUES AND OTHER FINANCING SOURCES	452,576	218,407	350,411
EXPENDITURES			
Current			
Food service	445,582	-	-
Athletics	-	208,661	-
Debt service			
Principal retirement	-	-	325,000
Interest, fiscal and other charges	-	-	26,635
Capital outlay	-	-	-
OTHER FINANCING USES			
Payments to escrow agent	-	-	-
TOTAL EXPENDITURES AND OTHER FINANCING USES	445,582	208,661	351,635
EXCESS OF REVENUES AND OTHER FINANCING SOURCES OVER (UNDER) EXPENDITURES AND OTHER FINANCING USES	6,994	9,746	(1,224)
Fund balances, beginning of year	15,458	5,430	57,764
Fund balances, end of year	\$ 22,452	\$ 15,176	\$ 56,540

Service Funds		Capital Projects Fund	Total Nonmajor Governmental Funds
Middle School Debt	Durant Bonds	Middle School	
\$ 672,246	\$ -	\$ 40	\$ 1,268,317
-	8,258	-	45,306
-	-	-	244,667
7,895,000	-	-	7,895,000
339,063	-	-	339,063
-	-	-	143,648
8,906,309	8,258	40	9,936,001
-	-	-	445,582
-	-	-	208,661
200,000	5,692	-	530,692
493,231	2,566	-	522,432
-	-	1,183	1,183
8,265,575	-	-	8,265,575
8,958,806	8,258	1,183	9,974,125
(52,497)	-0-	(1,143)	(38,124)
313,401	-	3,578	395,631
\$ 260,904	\$ -0-	\$ 2,435	\$ 357,507

Principals

Dale J. Abraham, CPA
Michael T. Gaffney, CPA
Steven R. Kirinovic, CPA
Aaron M. Stevens, CPA
Eric J. Glashouwer, CPA



ABRAHAM & GAFFNEY, P.C.

Certified Public Accountants

3511 Coolidge Road
Suite 100
East Lansing, MI 48823
(517) 351-6836
FAX: (517) 351-6837

**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

To the Board of Education
Montabella Community Schools
Edmore, Michigan

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Montabella Community Schools as of and for the year ended June 30, 2006, and have issued our report thereon dated August 3, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Montabella Community Schools' internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting that we have reported to administration of the District in a separate letter dated August 3, 2006.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Montabella Community Schools' financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance and other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to Management of Montabella Community Schools in a separate letter dated August 3, 2006.

This report is intended solely for the information and use of the management and Board of Education of Montabella Community Schools, the pass-through grantors, and the Federal awarding agencies and is not intended to be and should not be used by anyone other than these specified parties.

Abraham & Gaffney, P.C.

ABRAHAM & GAFFNEY, P.C.
Certified Public Accountants

August 3, 2006

East Lansing ■ Rochester Hills ■ St. Johns
- 30 -

Montabella Community Schools

**SUPPLEMENTARY INFORMATION
TO FINANCIAL STATEMENTS
(FEDERAL AWARDS)**

June 30, 2006

Montabella Community Schools

TABLE OF CONTENTS

June 30, 2006

Page

REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133	1-2
SUPPLEMENTARY INFORMATION	
Schedule of Expenditures of Federal Awards	3-4
Notes to Schedule of Expenditures of Federal Awards	5
REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS	6-7
SCHEDULE OF FINDINGS	8
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS	9

Principals

Dale J. Abraham, CPA
Michael T. Gaffney, CPA
Steven R. Kirinovic, CPA
Aaron M. Stevens, CPA
Eric J. Glashouwer, CPA



ABRAHAM & GAFFNEY, P.C.

Certified Public Accountants

3511 Coolidge Road
Suite 100
East Lansing, MI 48823
(517) 351-6836
FAX: (517) 351-6837

REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE
TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

To the Board of Education
Montabella Community Schools
Edmore, Michigan

Compliance

We have audited the compliance of Montabella Community Schools with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that is applicable to the major Federal program for the year ended June 30, 2006. Montabella Community Schools' major Federal program is identified in the summary of auditor's results section of the accompanying schedule of findings. Compliance with the requirements of laws, regulations, contracts and grants applicable to the major Federal programs are the responsibility of Montabella Community Schools' management. Our responsibility is to express an opinion on Montabella Community Schools' compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Nonprofit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on major Federal programs occurred. An audit includes examining, on a test basis, evidence about Montabella Community Schools' compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of Montabella Community Schools' compliance with those requirements.

In our opinion, Montabella Community Schools complied, in all material respects, with the requirements referred to above that are applicable to the major Federal programs for the year ending June 30, 2006.

Internal Control Over Compliance

The management of Montabella Community Schools is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to Federal programs. In planning and performing our audit, we considered Montabella Community Schools' internal control over compliance with requirements that could have a direct and material effect on the major Federal programs in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one (1) or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants caused by error or fraud that would be material in relation to the major Federal programs being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Montabella Community Schools as of and for the year ended June 30, 2006, and have issued our report thereon dated August 3, 2006. Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise Montabella Community Schools' basic financial statements. The accompanying schedule of expenditures of Federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

This report is intended solely for the information and use of the Board of Education and management of Montabella Community Schools, the pass-through grantors, and the Federal awarding agencies and is not intended to be used by anyone other than these specified parties.

Abraham & Gaffney, P.C.

ABRAHAM & GAFFNEY, P.C.
Certified Public Accountants

August 3, 2006

Montabella Community Schools

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Year Ended June 30, 2006

Federal Grantor / Pass-Through Grantor Program Title	Federal CFDA Number	Pass-Through Grantor's Number	Restated Program or Award Amount	(Memo Only) Prior Years' Expenditures	Balance July 1, 2005 Accrued or (Deferred) Revenue	Cash Receipts In-Kind Payments	Expenditures	Balance June 30, 2006 Accrued or (Deferred) Revenue
U.S DEPARTMENT OF EDUCATION								
Passed Through State Department of Education								
Title I Grants to Local Educational Agencies	84.010 ^(e)							
2004-05 Carryover		0515300506	\$ 49,379	\$ -	\$ -	\$ 49,379	\$ 49,379	\$ -0-
2004-05 Regular		0515300405	336,599	217,346	72,310	119,254	46,944	-0-
2005-06 Regular		0615300506	369,316	-	-	250,327	304,161	53,834
			755,294	217,346	72,310	418,960	400,484	53,834
Title V I.E.P.S.								
2004-05 Regular	84.298	0502500405	7,275	6,038	-	1,237	1,237	-0-
2005-06 Regular		0602500506	4,867	-	-	4,867	4,867	-0-
			12,142	6,038	-0-	6,104	6,104	-0-
Technology Literacy Challenge Grants								
2004-05	84.318	0542900405	9,809	9,809	3,410	3,410	-	-0-
2005-06		0642900506	6,890	-	-	4,192	6,303	2,111
			16,699	9,809	3,410	7,602	6,303	2,111
Comprehensive School Reform Demonstration								
2004-05	84.332	0418700405	90,405	76,164	4,099	18,340	14,241	-0-
2005-06		0518700506	94,000	-	-	79,485	90,369	10,884
			184,405	76,164	4,099	97,825	104,610	10,884
Improving Teacher Quality								
2004-05	84.367	0505200405	107,491	107,491	22,169	22,169	-	-0-
2005-06		0605200506	107,099	-	-	107,099	107,099	-0-
			214,590	107,491	22,169	129,268	107,099	-0-
Passed Through State Department of Education and Kent Intermediate School District								
Safe and Drug-Free Schools and Communities	84.186A							
2005-06		062860	8,242	-	-	4,050	4,050	-0-
TOTAL U.S. DEPARTMENT OF EDUCATION			1,191,372	416,848	101,988	663,809	628,650	66,829

Montabella Community Schools

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS - CONTINUED

Year Ended June 30, 2006

Federal Grantor / Pass-Through Grantor Program Title	Federal CFDA Number	Pass-Through Grantor's Number	Restated Program or Award Amount	(Memo Only) Prior Years' Expenditures	Balance July 1, 2005 Accrued or (Deferred) Revenue	Cash Receipts In-Kind Payments	Expenditures	Balance June 30, 2006 Accrued or (Deferred) Revenue
U.S. DEPARTMENT OF AGRICULTURE								
Passed Through State Department of Education								
National School Breakfast Program	10.553 ^(f)							
2004-05		051970	\$ 64,514	\$ 57,719	\$ -	\$ 6,795	\$ 6,795	\$ -0-
2005-06		061970	57,176	-	-	57,176	57,176	-0-
			121,690	57,719	-0-	63,971	63,971	-0-
National School Lunch Program	10.555 ^(f)							
2004-05		051950,051960	163,719	143,716	-	20,003	20,003	-0-
2005-06		061950,061960	146,486	-	-	146,486	146,486	-0-
			310,205	143,716	-0-	166,489	166,489	-0-
Food Donation ^{(a) (c)}	10.550	59045						
Entitlement commodities								
2005-06			13,893	-	-	13,893	13,893	-0-
Bonus commodities								
2005-06			314	-	-	314	314	-0-
			14,207	-0-	-0-	14,207	14,207	-0-
TOTAL U.S. DEPARTMENT OF AGRICULTURE			446,102	201,435	-0-	244,667	244,667	-0-
TOTAL FEDERAL AWARDS			\$ 1,637,474	\$ 618,283	\$ 101,988	\$ 908,476 ^(d)	\$ 873,317 ^(b)	\$ 66,829

Montabella Community Schools

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

June 30, 2006

NOTE A: BASIS OF PRESENTATION

The accompanying Schedule of Expenditures of Federal Awards includes the Federal grant activity of Montabella Community Schools and is presented on the modified accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Nonprofit Organizations*.

NOTE B: SUMMARY OF SIGNIFICANT EXPLANATIONS OF SCHEDULE

The following descriptions identified below as (a) through (f) represent explanations that cross reference to amounts on the Schedule of Expenditures of Federal Awards.

- (a) The current year revenues for the Food Donation Program are determined based on the 2002/03 guidance provided in the Michigan Department of Education Administrative Policy Number 7. The amounts reported in this schedule as commodities received were taken from the Recipient Entitlement Balance Report, which are in agreement in all material respects with the District's reported amounts.
- (b) The expenditures reported in this schedule are in agreement with the amounts reported in the financial statements and financial reports. The financial reports tested, including claims for advances and reimbursements, were materially correct, complete, accurate, and timely and contain information that is supported by the books and records from which the financial statements have been prepared.
- (c) The amount of out of conditioned commodities due to spoilage or shrinkage included in expenditures is immaterial to the Schedule of Expenditures of Federal Awards taken as a whole.
- (d) The amounts reported in this schedule as cash received are in agreement with the current payment amounts in the Grants Section Auditor's Report.
- (e) Denotes program tested as "major program".
- (f) Denotes programs required to be clustered by the United States Department of Agriculture.

NOTE C: RECONCILIATION TO FINANCIAL STATEMENTS

The following reconciles the federal revenues reported in the June 30, 2006 Basic Financial Statements to the expenditures of the District administered federal programs reported on the Schedule of Expenditures of Federal Awards.

	<u>General Fund</u>	<u>Special Revenue Funds</u>	<u>Total</u>
Revenues from federal sources per financial statements	\$ 674,244	\$ 244,667	\$ 918,911
Less: Medicaid Assistance not subject to single audit	(45,594)	-	(45,594)
Federal expenditures per Schedule of Expenditures of Federal Awards	<u>\$ 628,650</u>	<u>\$ 244,667</u>	<u>\$ 873,317</u>

Principals

Dale J. Abraham, CPA
Michael T. Gaffney, CPA
Steven R. Kirinovic, CPA
Aaron M. Stevens, CPA
Eric J. Glashouwer, CPA



3511 Coolidge Road
Suite 100
East Lansing, MI 48823
(517) 351-6836
FAX: (517) 351-6837

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

Board of Education
Montabella Community Schools
Edmore, Michigan

We have audited the financial statements of Montabella Community Schools as of and for the year ended June 30, 2006, and have issued our report thereon dated August 3, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Montabella Community Schools' internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one of more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Montabella Community Schools' financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that were reported to management of Montabella Community Schools in a separate letter dated August 3, 2006.

This report is intended for the information and use of the Board of Education and management of Montabella Community Schools, the pass-through grantors, and Federal awarding agencies and is not intended to be and should not be used by anyone other than these specified parties.

Abraham & Gaffney, P.C.

ABRAHAM & GAFFNEY, P.C.
Certified Public Accountants

August 3, 2006

Montabella Community Schools

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Year Ended June 30, 2006

Section I - Summary of Auditor's Results

Financial Statements

Type of auditor's report issued: Unqualified

Internal control over financial reporting:

Material weakness(es) identified? _____ Yes X No

Reportable condition(s) identified that are not considered to be material weakness(es)? _____ Yes X None reported

Noncompliance material to financial statements noted? _____ Yes X No

Federal Awards

Internal control over major programs:

Material weakness(es) identified? _____ Yes X No

Reportable condition(s) identified that are not considered to be material weakness(es)? _____ Yes X None reported

Type of auditor's report issued on compliance for major programs: Unqualified

Any audit findings disclosed that are required to be reported with Section 501(a) of Circular A-133? _____ Yes X No

Identification of major programs:

CFDA Number(s)	Name of Federal Program or Cluster
84.010	Title I

Dollar threshold used to distinguish between Type A and Type B programs: \$ 300,000

Auditee qualified as low-risk auditee? X Yes _____ No

Section II - Financial Statement Findings

None

Section III - Federal Award Findings and Questioned Costs

None

Montabella Community Schools

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

Year Ended June 30, 2006

There were no findings disclosed for the past two years.

Principals

Dale J. Abraham, CPA
Michael T. Gaffney, CPA
Steven R. Kirinovic, CPA
Aaron M. Stevens, CPA
Eric J. Glashouwer, CPA



3511 Coolidge Road
Suite 100
East Lansing, MI 48823
(517) 351-6836
FAX: (517) 351-6837

MANAGEMENT LETTER

To the Board of Education
Montabella Community Schools
Edmore, Michigan

As you know, we have recently completed our audit of the records of Montabella Community Schools as of and for the year ended June 30, 2006. In connection with the audit, we feel that certain changes in your accounting and administrative procedures would be helpful in improving management's control and the operational efficiency of the accounting and administrative functions. These suggestions are a result of our evaluation of the internal control structure and our discussions with management.

1. The District should review various areas of operation and consider additional segregation of duties.

During our consideration and assessment of fraud risk, we noted that the District may not have sufficient segregation of duties in its accounting structure (centralized and decentralized). The intent of internal control is to assure that no one individual is able to control all aspects of a transaction cycle (i.e., receipts, disbursements, etc.). This issue was noted and reported in our audit comments last year.

While this is a common occurrence in small Districts due to the limited number of employees, the District should realize that a greater risk in safeguarding assets exists if duties and responsibilities are not appropriately arranged and separated.

The Board of Education should realize that given the limited number of employees involved in each of the decentralized activities, the District is assuming a greater risk of loss or misappropriation related to the activities accounts.

We suggest that the District review various areas of operation and consider additional segregation of duties. If duties cannot be adequately segregated due to the limited number of employees, we suggest the District management provide a greater review and supervision of employee functions and procedures.

2. The District should monitor and limit the use of its name and/or employer identification number.

During the course of our audit, we noted that several organizations/entities independent of the District (i.e., PTO, Junior Achievement, boosters, etc.) hold deposit accounts with local banks under the name and/or employer identification number of the District. This issue was noted and reported in our audit comments last year.

It is our understanding that the PTO organization is currently in the process of obtaining its own employer identification number.

We suggest the District contact the banks with which it does business and take the necessary steps to have the District's identifying information removed from all accounts not under the control of the District.

These conditions were considered in determining the nature, timing, and extent of the audit tests to be applied in our audit of the basic financial statements, and this report does not affect our report on the basic financial statements dated August 3, 2006.

This report is intended solely for the information and use of the administration of Montabella Community Schools, and should not be used for any other purpose.

We wish to express our appreciation for the courtesy and cooperation extended to us during our audit. We are available to discuss any or all of these suggestions with you and to provide assistance in the implementation of improvements.

Abraham & Gaffney, P.C.

ABRAHAM & GAFFNEY, P.C.
Certified Public Accountants

August 3, 2006